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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1956.

**No. 323**

H. C. HAMMER, MORRIS NORIAN AND RICHARD NORIAN,

*Petitioners,*

*vs.*

CHARLES W. SANDERS, JOHN L. FYE AND O. R. THOUREEN, INDIVIDUALLY AND AS CO-PARTNERS DOING BUSINESS AS THE SANDERS-FYE DRILLING COMPANY,

*Respondents.*

## PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF ILLINOIS.

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THE GUNTHORP-WARREN PRINTING COMPANY, CHICAGO 56

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*Respondents.*

---

## PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF ILLINOIS.

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Petitioners, H. C. Hammer, Morris Norian, and Richard Norian, the plaintiffs, pray that a writ of certiorari issue to review the judgment of the Supreme Court of Illinois.

### OPINION BELOW.

The opinion of the Illinois Supreme Court is officially reported at 8 Ill. 2d 414, 134 N. E. 2d 509. The dissenting opinion of three of the seven judges commences at 8 Ill. 2d 425, 134 N. E. 2d 515. Appendix B of this petition contains the majority opinion at pages iii to xiv, and the dissenting opinion at pages xv to xxi. Both opinions are also contained in the certified record at pages 7 to 19.

## JURISDICTION.

The judgment of the Illinois Supreme Court, a copy of which is contained in Appendix B to this petition, was entered on March 22, 1956. (R. 20-21.) Rehearing was denied on May 22, 1956. (R. 24.)

The jurisdiction of this court is invoked under the Judicial Code, 62 Stat. 929, 28 U. S. C. 1257(3).

## QUESTION PRESENTED.

Petitioners are investors. Respondents are promoters and drillers of oil wells. The question is whether forty-five fractional undivided interests in oil and gas leases, which respondents sold to petitioners, are securities under the Federal Securities Act of 1933; or whether they are outside the definition of securities because respondents artfully cast them not merely as sales of fractional undivided interests but also as "drilling agreements".

Three justices of the Illinois Supreme Court held that the instruments were securities under the definition of the Federal Securities Act of 1933. Four justices denied relief to petitioners, refraining from considering the Federal question although petitioners' raising of the Federal question was timely and proper.

## STATUTE INVOLVED.

The pertinent portions of the Federal Securities Act of 1933 are:

1. Section 2(1) of the Federal Securities Act of 1933, Tit. I § 2(1), 48 Stat. 74, 905, 15 U. S. C. 77(b)(1):

> The term "security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorgan-

ization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

2. Section 2(3) of the Federal Securities Act of 1933, Tit. I § 2(3), 48 Stat. 74, 15 U. S. C. 77(b)(3):

> * * * Any security given or delivered with, or as a bonus on account of, any purchase of securities or any other thing, shall be conclusively presumed to constitute a part of the subject of such purchase and to have been sold for value. * * *

## STATEMENT OF THE CASE.

This case is a consolidation of three actions instituted by petitioners. In fifty-one separate transactions between May 26 and October 24, 1952, respondents through their salesmen and solicitors sold to petitioners unregistered fractional undivided interests in oil and gas leases for amounts totaling $78,596.40. Except for two invoices covering six interests (R. 2:42, 2:108), respondents effected each sale of securities by letter agreements which were identical in form, differing only as to date, location of the oil and gas lease, amount of the fractional interest sold, and money consideration. One of the letter agreements appears in the majority opinion at pages iv-v of Appendix B. Respondents retained a one-fourth fractional interest in each lease (R. 2:129-130), and sold all remaining fractional interests to numerous investors whose identity they refused to disclose even upon deposition in the trial court. (R. 2:166-170.)

For money consideration, each letter agreement expressly sold to the investor an undivided fractional working interest in an oil and gas lease "for investment purposes only," and at the same time included respondents' agreement to drill for oil to a specified depth. The same money consideration served for both the drilling and the purchase of the undivided fractional oil and gas lease interest. The investor had no further obligation at all, unless a producing well came in. Then the investor was to be charged with his share of the expense of completing and operating the well. For each one of the fifty-one interests sold, respondents invoiced petitioners for a "working interest". (R. 2:10-43, 2:57-64, 2:77-110.) Of the 51 separate sales, 39 were dry holes, representing most of petitioners' investments.

Under both the Federal Securities Act of 1933 and the Illinois Securities Law, petitioners tendered all interests back to respondents, and respondents refused the tenders. Petitioners then filed actions under both the Illinois and Federal Securities Acts to recover the amounts paid. The trial court gave judgment for the petitioners. On appeal, however, the Illinois Appellate Court reversed the judgment, holding that the transactions were not sales of securities and that there was no proper tender. (6 Ill. App. 2d 346, 127 N. E. 2d 492.) The Illinois Supreme Court granted leave to appeal.

The Illinois Secretary of State, who is charged with the administration and enforcement of the Illinois Securities Law, obtained permission to appear as *amicus curiae* on the ground of major public importance, and urged the Illinois Supreme Court to find that the letter agreements were securities.

As to forty-five of the fifty-one sales, the Illinois Supreme Court affirmed the judgment of the Appellate Court,

and held that the letter agreements were not securities under the Illinois Securities Law. As to the six transactions covered by two invoices and not by letter agreements, the Illinois Supreme Court held that they were sales of securities under the Illinois Securities Law. The majority opinion refrained from passing on whether the letter agreements were securities under the Federal Securities Act of 1933.

**HOW FEDERAL QUESTION IS PRESENTED.**

A Federal question was properly raised by petitioners' complaints at the moment they were filed in the court of first instance, the Circuit Court of Cook County, Illinois. The complaints consisted of two counts. Count I alleged that the transactions violated the Illinois Securities Law (R. 2:1-6, 2:49-54; 2:68-74), and Count II, which is contained in Appendix C to this petition, alleged that the transactions violated the Federal Securities Act of 1933. (R. 2:7-8; 2:54-55; 2:74-75.)

The majority Illinois opinion below expressly states (Appendix B vi):

> "By their complaints, filed in February, 1953, the plaintiffs sought to rescind the transactions and recover all sums expended by them. They alleged a violation of both the Illinois Securities Act of 1919 *and the Federal Securities Act of 1933.*" (Emphasis supplied.)

Nevertheless, the majority Illinois opinion failed to consider the violation of the Federal Securities Act of 1933. Its failure to do so is commented upon in the dissenting opinion (Appendix B xv) as follows:

> "* * * nor (can we) understand their (majority of the court) failure to consider the charge of violation of the Federal Securities Act, as alleged in Count II

of the complaint and assigned as error and so argued by plaintiffs. These transactions cannot be placed outside the purview of the State or Federal Securities Acts without ignoring the plain language of the statutes and the clear economic import of the transactions."

## REASONS FOR GRANTING THE WRIT.

### 1. The Illinois Decision Creates a Serious Public Enforcement Problem. If It Stands, It Would Permit Easy Circumvention of the Federal Securities Act of 1933 in Sales of Oil Securities.

Oil and gas ventures are particularly vulnerable to irresponsible promotions upon a credulous or ignorant public. The history of the exploitation of oil and gas rights is one of great commercial and economic development, with concurring wildcat speculation and fraudulent and deceitful promotions.

The Illinois decision construing the definition of "security" as it affects contracts for exploiting oil presents a matter of major public importance in the administration and enforcement of the Federal Securities Act. If it is allowed to stand, the Illinois decision creates a simple method to circumvent the plain requirements of the Act in the sale of oil securities. Urgent and compelling considerations of public policy make it necessary that the writ be granted.

The majority Illinois opinion, by its hyper-technical and basically impractical analysis of the transactions before the Court, would create a potentially powerful instrument for fraudulent promotions to bilk the public. It would serve judicially to abrogate the clear language and intention of the Congress and to foster the abuses which Congress intended to end.

**2. In the Sale of Oil Securities, Promoters Have Devised a Great Variety of Forms, Which the Federal Securities Act of 1933 Was Designed to Regulate. Respondents' Device Is Clearly Within the Terms of the Act.**

Methods of oil and gas financing by the sale of securities have assumed a great variety of forms devised by the ingenuity and shrewdness of blue sky violators. By the breadth of the language used, Congress sought to bring the widest variety of security sales within the Act, and to prevent the unregulated use of devious and ingenious schemes. This Court itself has said that oil and gas rights have been such notorious subjects of speculation and fraud that they posed a difficult problem for the legislative draftsman. *Securities & Exchange Commission* v. *Joiner*, 320 U. S. 344, 352.

As illustrations of the breadth of the devices which courts have brought under securities laws, we have compiled in Appendix A a tabulation of forms used by oil and gas promoters which have come under appellate judicial scrutiny, and of the court decisions which have passed on them. The forms used by defendants to sell their oil securities clearly fall under the Act.

Congress intended to encompass all sales of oil securities by the definition in the Act. Short of a word by word description of every wildcat scheme that might be imagined by promoters to separate an investor from his money, it is difficult to see how the draftsmen of the Act could have described the instrument in question more clearly than a "fractional undivided interest in oil, gas, or other mineral rights." By judicial gloss and contrary to the legislative intent, the Illinois Supreme Court has excised an entire class of dealing from the plain language of the Act. Without indicating in any way that the language is vague, indefinite, or void, the Illinois court merely disregarded it.

### 3. Respondents' Simultaneous Sale of the Oil Security and Their Agreement to Drill a Well, Both for the Same Money Consideration, Constitute a Sale of a Security Under the Act, and Not a "Drilling Agreement" Outside the Act.

The letter agreements, artfully drafted by the defendants, are securities within the definition of the Act. They expressly refer to the acquisition and assignment for money of undivided working interests in oil and gas leases "for investment purposes only," as both parties stated.

Nevertheless, the majority Illinois opinion held that the transactions were not sales of securities because the development contract aspects of the instruments were "uppermost" in the minds of the parties and the money which petitioners paid was for drilling costs and not for the purchase of undivided fractional interests in oil and gas leases. The majority view is hardly a realistic one.

As the Illinois dissenting opinion points out (Appendix B xix), petitioners invested money for undivided fractional interests and with the understanding that respondents would drill wells. But the drilling of the well, in itself, would benefit petitioners not at all unless they received, for their investment, a right to share in the oil benefits reaped by the drilling efforts. There was no provision in the letter agreement for any further payment to acquire a fractional undivided working interest, since the letter agreement itself constituted such a sale. The only additional provision was to bear a proportionate part of well expenses if a producing well ensued.

The Illinois decision is in direct conflict with the applicable holdings of this Court in *Securities & Exchange Commission* v. *Howey Co.*, 328 U. S. 293, and *Securities & Exchange Commission* v. *Joiner*, 320 U. S. 344. In language

which applies forcefully to the instruments in this case, this Court stated in the *Joiner* opinion:

> It is clear that an economic interest in this well-drilling undertaking was what brought into being the instruments that defendants were selling and gave to the instruments most of their value and all of their lure. The trading in these documents had all the evils inherent in the securities transactions which it was the aim of the Securities Act to end. (P. 349.)

Even if it be assumed, as the Illinois majority opinion says, that "at best, the transfer of a working interest was incidental to the development contract" (Appendix B xi), the Illinois majority conclusion is contrary to the provisions of Section 2(3) of the Federal Securities Act, quoted above at page 3.

In effect, the Illinois majority opinion states:

> The money was for drilling costs. The fractional undivided oil and gas lease interests were free. Therefore, there was no sale of securities.

If this doctrine prevailed, the Act could be circumvented by the most obvious devices. In any sale of oil securities, the consideration could easily be ascribed to any related aspect other than the security, and the Act would be avoided.

It was precisely to prevent the situation which as now arises under the Illinois majority opinion, that Congress provided in Section 2(3) a conclusive presumption, regardless of what aspect is "uppermost" in the minds of the parties. In the instant case, the conclusive presumption legally ascribes the "consideration paid" to the sales of working interests and not to drilling costs.

In discussing Section 2(3) of the Act, Loss on Securities Regulation (1951) says:

> "Bonus" Stock: Section 2 (3) makes specific what

> would probably have been the construction in any event: "Any security given or delivered with, or as a bonus on account of, any purchase of securities or any other thing, shall be conclusively presumed to constitute a part of the subject of such purchase and to have been sold for value." This is another way of stating the obvious proposition that, when a drug store gives a second tube of toothpaste "free" with every tube purchased for 50 cents, the cost is 25 cents per tube. (P. 332.)

See also *Whittaker* v. *Wall*, 226 F. 2d 868 (C. A. 8—1955).

If the controlling mandate of the Act were paraphrased to apply to the instant case, it would read:

> Any working interest given or delivered with, or as a bonus on account of payments made for drilling costs, shall be conclusively presumed to constitute a part of the subject of such purchase and to have been sold for value.

A judicial nullification of the statute would cause the utmost confusion and maladministration.

The trial court heard this cause on motions for summary judgment. Petitioners' affidavits for summary judgment expressly state that respondents sold the issues of oil securities in interstate commerce and by use of the mails and that the sales of the securities were not exempt. (R. 2:118 incorporating 2:1-49; 2:121 incorporating 2:68-117; and 2:125 incorporating 2:49-68.) Respondents had no affidavits nor motions in opposition to petitioners' motions for summary judgment. (R. 2:171-172.) In their own affidavits in support of their motion for summary judgment, respondents did not controvert petitioners' affidavits as to interstate commerce, use of the mails, or non-exemption. (R. 2:129-161.)

In Illinois on motion for summary judgment the supporting and opposing affidavits are controlling and the fact

that the pleadings join issue does not prevent the entry of a summary judgment. Petitioners' uncontradicted allegations in their affidavits are the undisputed facts of this case. To have prevented the entry of a summary judgment, respondents were obliged to file a sufficient affidavit of defense. This they failed to do. (*Killian* v. *Welfare Engineering Co.*, 328 Ill. App. 375, 384-385, 66 N. E. 2d 305, 310; *Roberts* v. *Sauerman Bros.*, 300 Ill. App. 213, 216-217, 20 N. E. 2d 849, 850.)

Respondents admittedly failed to register their securities. Respondents also failed to comply in any way with the information requirements of the liberal exemption which the Securities & Exchange Commission has granted to small issues of oil and gas securities (Securities & Exchange Commission, General Rules and Regulations, Regulation B, Rules 300 and 320, 2 Fed. Reg. 904-905, 13 CFR 230.300 and 230.320 (1937)) and which is conditioned upon the prior deposit of minimum information with the Commission.

That the instruments before the Court are securities is clearly shown by the definition of "working interests" which the Securities and Exchange Commission published on November 27, 1939, and has adhered to ever since. In its Form S-10 and instructions for registration of oil or gas interests under the Federal Securities Act of 1933, the Commission expressly made the following definition:

> The term "working interests" means fractional undivided interests in an oil or gas leasehold which are subject to any portion of the expense of *development*, operation, or maintenance.

(Emphasis supplied. Commerce Clearing House Federal Securities Law Reporter, vol. 1, pars. 7201-7202, p. 3691.)

**Tax Treatment Does Not Abrogate Securities Act.**

In order to encourage the flow of capital into the development of oil and gas resources, Congress has provided certain tax advantages which have greatly stimulated public purchases of oil and gas securities. Congress did not intend that tax laws or regulations should repeal the plain requirements of the Federal Securities Act of 1933. The fact that the taxpayer-investor may expense intangible drilling and development costs does not mean that Congress intended that oil and gas investments should be made on an uninformed basis. (Bloomenthal, S. E. C. Aspects of Oil and Gas Financing, 7 Wyo. L. J. (1953) 49, 63; Bloomenthal, A Guide To Federal Oil and Gas Income Taxation, 8 Wyo. L. J. (1954) 83, 97.)

Respondents pre-cast the instruments before the Court so as to achieve maximum benefits under the Internal Revenue Code. However, neither a tax consideration nor a promoter's device should subvert the public interest in adequately regulating oil securities. This Court looks to the substance of the transaction—the sale of a fractional undivided interest in an oil lease.

**CONCLUSION.**

One can hardly imagine a more flagrant enactment of judicial exemption than the Illinois majority opinion. If it stands, many, many of millions of dollars in oil and gas securities would escape all regulation under the Federal Securities Act of 1933. Administration of the Act would be in the utmost confusion. Clear sales of oil and gas securities would gain exemption whenever the seller would merely state that the consideration is going for some related purpose. The decision of the Illinois Supreme court ought to be reviewed.

The instruments before the Court are clearly sales of securities. Petitioners pray that a writ of certiorari be granted.

Respectfully submitted,

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*Counsel for Petitioners.*

IRA S. KOLB,
*Of Counsel.*

August 17, 1956.

## APPENDIX A.

### Tabulation of Devices Used by Oil and Gas Promoters Which Have Been Held to Be Securities Under Securities Acts.

| DEVICE | NAME AND CITATION OF CASE |
|---|---|
| Assignment of lease plus test-well drilling agreement. | *Securities & Exchange Commission* v. *Joiner Corp.*, 320 U. S. 344.<br>*Price* v. *U. S.*, 200 F. 2d 652 (CA 5, 1953). |
| Contract for equipment and drilling expense. | *Whittaker* v. *Wall*, 226 F. 2d 868 (CA 8, 1955). |
| Warranty deed to land, plus agreement that wells were being and would be drilled thereon. | *Mansfield* v. *U. S.*, 155 F. 2d 952 (CA 5, 1946). |
| Partial assignments of leases plus undivided interests in a drill site. | *Atherton* v. *U. S.*, 128 F. 2d 463 (CA 9, 1942). |
| "Mineral Deeds." | *Barnhill* v. *Young*, 46 F. 2d 804 (1931 D. C. Cal.). |
| | *People* v. *Jackson*, 24 Cal. App. 2d 182, 74 P. 2d 1085 (1937). |
| | *People* v. *Blankenship*, 305 Mich. 79, 8 N. W. 2d 919 (1943). |
| | *Moore* v. *Stella*, 52 Cal. App. 2d 766, 127 P. 2d 300 (1942). |
| "Deeds." | *People* v. *Yant*, 26 Cal. App. 2d 725, 80 P. 2d 506 (1938). |
| "Mineral Deeds" and "Transfer Orders." | *State* v. *Pullen*, 58 R. I. 294, 192 A. 473 (1937). |
| Deed plus declaration of trust. | *People* v. *McCalla*, 63 Cal. App. 783, 220 P. 436 (1923); writ of error dismissed, 267 U. S. 585 (1925). |

| DEVICE | NAME AND CITATION OF CASE |
|---|---|
| "Units" and "Grant Deeds." | *People* v. *Daniels*, 25 Cal. App. 2d 64, 7 P. 2d 556 (1938). |
| Certificates of beneficial interest in trust holding oil and gas leases. | *Young* v. *Three for One Oil Royalties*, 1 Cal. 2d 639, 36 P. 2d 1065 (1934). |
| "Units" of beneficial interest in trust holding oil and gas leases (proceeds to go to drill wells). | *Barrett* v. *Gore*, 88 Cal. App. 372, 263 P. 564 (1928). |
| Sale of interest in oil producing project plus option to buy oil and gas lease assignment. | *People* v. *Rubens*, 11 Cal. App. 2d 576, 54 P. 2d 98 (1936). |
| Certificates for overriding royalty interests (proceeds to be used for drilling well). | *O'Connell* v. *Union Drilling & Petroleum Co.*, 121 Cal. App. 302, 8 P. 2d 867 (1932). |
| Promissory note for amount of loan, plus percentage of future-produced oil and gas. | *People* v. *Sidwell*, 27 Cal. 2d 121, 162 P. 2d 913 (1945). |
| Percentage of oil and gas production. | *Domestic & Foreign Petroleum Co.* v. *Long*, 4 Cal. 2d 547, 51 P. 2d 73 (1935). |
| "Partnership Profit-Sharing Agreement" and "Guaranteed Re-sale Lease Agreement." | *Ryan* v. *State*, 128 Fla. 1, 174 So. 43 (1937). |
| "Statement and Purchase" (money to be placed in fund to be used to exploit oil leasehold). | *State* v. *Ogden*, 154 Minn. 425, 191 N. W. 916 (1923). |
| "Service Contract" and sale of oil pumps to be used in exploiting leasehold. | *Rice* v. *Bogart*, 272 Ill. App. 292 (1933). |
| Transfer of "1/32 of a pipeline interest in 7/8 of 160 acres" plus agreement to drill a well, subject to obligations if a producing well is found. | *State* v. *Walters*, 244 Iowa 1253, 58 N. W. 2d 4 (1953). |

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## OPINIONS OF ILLINOIS SUPREME COURT.

(Rehearing Denied May 22, 1956.)

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Mr. Chief Justice Hershey delivered the opinion of the court:

In the circuit court of Cook County, the plaintiffs, H. C. Hammer, Morris Norian and Richard Norian, obtained judgments against the defendants, Charles W. Sanders, John L. Fye and O. R. Thoureen, individually and as co-partners doing business as the Sanders-Fye Drilling Company, for sums paid the latter pursuant to 51 separate oil transactions. The judgments were for $40,328.18, $31,279.86 and $6,988.36, respectively.

The plaintiffs successfully maintained in the trial court that the money was for the purchase of "securities" within the meaning of section 2 of the Illinois Securities Act of 1919 (Ill. Rev. Stat. 1953, chap. 121½, par. 97,) and since the defendants had not complied with this statute relative to registration, etc., the sales could be rescinded and, upon tender, the consideration paid, plus reasonable attorney's fees, could be recovered. Ill. Rev. Stat. 1953, chap. 121½, par. 132.

On appeal, the Appellate Court reversed, holding both that the transactions did not involve the sale of "securities" within the statutory definition and that there was no proper tender. (See 6 Ill. App. 2d 346.) We allowed petition for leave to appeal and granted the Secretary of State permission to appear as *amicus curiae*.

The cause was heard on motions for summary judgment, and for the most part the facts are undisputed.

CLOSE IN CENTER

The defendants, who were in the oil business as partners under the name of Sanders-Fye Drilling Company, owned oil leases in Indiana, Illinois and Kentucky. During the summer of 1952 they concluded 51 separate transactions with the plaintiffs relative to developing these leases, 45 of which were based on so-called letter agreements and six of which were evidenced by invoices only. The letter agreements were identical in form, differing merely as to date, location of property, amount of interest, and sums of money due. For reference, we quote one of these instruments in full:

"Sanders-Fye Drilling Co.
Contractors—Oil Producers
Lamkin Building
Olney, Illinois

Date ....June 15, 1952....
Re....Sec. 29, 38-13W....
Gibson Indiana
County State

*Mr. Hy Hammer*
*Hammer Bros.*
*33 N. Western Ave.*
*Chicago 12, Ill.*

DEAR SIR:

This letter will confirm our understanding regarding your acquisition of an interest in leases on property as set forth below.

We will assign to you an undivided....1/128th.... working interest, under oil and gas leases on a block of ....200....acres, located in ....Gibson....County, ....Indiana...., for the sum of $....242.19.....

We agree to commence or cause to be commenced, upon the leasehold estate described above, the drilling of a well for oil and/or gas, to diligently prosecute the drilling of same and to test all possible oil forma-

tions encountered to a depth of approximately.... 3000....feet, unless oil or gas in commercial quantities is discovered at a lesser depth, for the sum of $....242.19...., which is your share of the drilling cost of this well. We will plug the well should it be a dry hole.

In the event of a producing well, it is understood and agreed that, in addition to the amount as set out above, you will pay your proportionate part of the casing, drilling in expense, and for all equipment necessary to complete the well, as well as your proportionate part of the monthly operating expense, upon receipt of invoice. It is also understood that for any additional wells that might be drilled, you will pay your proportionate part of all costs, which costs may include the normal drilling profit of Sanders-Fye Drilling Company.

It is agreed that each individual co-owner retains the right to revoke at will the operator's power to sell such co-owner's oil and also denies the operator the power to enter into any contract beyond the minimum needs of the industry under the circumstances and in any event in excess of one year.

It is also agreed that you are purchasing this interest for investment purposes only without any present intention of reselling this interest.

If this is your understanding of our agreement, kindly signify your acceptance by signing in the space provided below and return one copy to this office.

Very truly yours,

SANDERS-FYE DRILLING COMPANY,
By...../s/ JOHN L. FYE.....
*Partner*

Accepted
..../s/ HY HAMMER.....
....July 21, 1952....."

In each instance, drilling was either in progress at the time the instrument was signed or commenced shortly thereafter. Shares ranged from 1/256th to 1/8th.

The first six transactions involved the drilling on an Indiana lease, and oil was discovered there in paying quantities. For these, the defendants then executed written assignments, covering the interests specified in said letter agreements.

In six other transactions, there was also oil production. But these differed from the others. A dispute arose in which the plaintiffs claimed that one of the defendants' agents had guaranteed there would be production from a certain well, but it turned out to be a dry hole. While maintaining that the agent had no authority to make any such guarantee, the defendants said they would assign to them, at defendants' cost, interest in another lease where there was production. The transactions are evidenced by written invoices billing the plaintiffs for the cost, which they paid. No written assignments had been executed as of the time the instant suits were filed.

In all other cases, involving seven different leases, drilling resulted in dry holes and no assignments were made or further action taken.

By their complaints, filed in February, 1953, the plaintiffs sought to rescind the transactions and recover all sums expended by them. They alleged a violation of both the Illinois Securities Act of 1919 and the Federal Securities Act of 1933. The defendants disputed their right to recover, and as presented and argued, the issue is twofold: (1) Were the instruments or interests involved securities which were sold in violation of the Illinois statute? (2) If so, did the plaintiffs make proper statutory tender?

The applicable provisions of the Illinois Securities Law of 1919 are as follows:

"The word 'securities' shall mean * * * any oil, gas or mining lease, royalty, or deed, and interest, units or shares in any such lease, royalty, or deed * * * 'sale' * * * shall include every disposition, or attempt to dispose, of a security or interest in a security for value. The term 'sale' means and includes contracts and agreements whereby securities are sold, traded or exchanged for money, property or thing of value, or any transfer or agreement to transfer, in trust or otherwise." Ill. Rev. Stat. 1953, chap. 121½, par. 97.

"Every sale and contract of sale made in violation of any of the provisions of this Act shall be void at the election of the purchaser, and the seller of the securities so sold * * * shall be * * * liable, in an action at law or in equity, upon tender to the seller or in court of the securities sold, to the purchaser for the amount paid, the consideration given or the value thereof, together with his reasonable attorney's fees in any action brought for such recovery." Ill. Rev. Stat. 1953, chap. 121½, par. 132.

We discuss initially those transactions evidenced by an instrument of the type set out above. In this regard, we must analyze the terms of the instrument with a view to determining, at least in a general way, its legal effect.

It appears that Sanders-Fye Drilling Company and Hy Hammer had some understanding as to the latter's acquiring an "interest" in the designated leases, and this letter is sent to confirm (or, more properly, to effectuate) that understanding.

Considered in its entirety, the instrument seems to have two purposes: (1) to assign or evidence the sale of or

promise to assign, an undivided 1/128th "working interest" in the leases to Hammer for $242.19; (2) to evidence an agreement whereby Sanders-Fye is to drill a test well and Hammer is to pay $242.19 as his share of the cost, with a further provision for the payment of his "proportionate part" in equipping and operating a producing well and in drilling additional wells.

Hammer's "proportionate part" of this additional expense is obviously meant to be 1/128th, his share of the working interest. Likewise, the amount of oil to which he is to be entitled is determined by his share in the working interest. Assuming the usual 1/8th royalty to the lessor, this would give Hammer a 1/128th undivided interest in 7/8th of the oil produced. Cf. *Fry* v. *Farm Bureau Oil Co.*, 3 Ill. 2d 94, 95; *Illinois National Oil and Gas Co.* v. *Sinclair*, 373 Ill. 581, 582.

On its face, then, the instrument involves the sale of an undivided 1/128th working interest in the leases, coupled with or forming a part of a development contract to procure a test of the land for oil and gas. (See Summers, The Law of Oil and Gas, vol. 4, sec. 722.) Nothing further appearing, it would seem that this sale of a 1/128th working interest in the leases for the sum of $242.19 amounted to the sale of an "interest" in an oil "lease" within the purview of the Illinois statute and hence a "security." (Cf. *Securities Exchange Com.* v. *Joiner Corp.*, 320 U. S. 344; *People* v. *Craven*, 219 Cal. 522; *Commonwealth* v. *Yaste*, 166 Pa. Super. 275.) However, while the terms of the instrument apparently call for the payment of two identical sums, just one sum was actually paid. And this was regarded by the parties as the only amount due. Thus, Hammer did not pay $242.19 for the undivided 1/128th working interest and another $242.19

for drilling costs. Rather, he paid $242.19 only, and by his own admission this was for drilling costs alone, as provided in the third paragraph of the instrument.

When we thus consider performance, we discover what appears to be a conflict between the import of the instrument and the parties' own understanding of its terms. That such should arise, however, is not surprising in view of the varying interpretations which might with some justification be urged. Were there to be two payments, one for the working interest (second paragraph) and another for drilling costs (third paragraph)? On its face, this is certainly a reasonable interpretation. But, as the minority suggest, it might be that only one payment is contemplated. The foregoing, in our opinion, brings to light an ambiguity or uncertainty which we may attempt to clarify by considering extrinsic evidence. And "in the determination of the meaning of an indefinite or ambiguous contract, the interpretation placed upon the contract by the parties themselves is to be considered by the court and is entitled to great, if not controlling, influence in ascertaining their understanding of its terms." 12 Am. Jur., Contracts, sec. 249, pp. 787-8. See also 12 I.L.P., Contracts, sec. 244.

The practice of the parties is enlightening. Sanders-Fye, a drilling company, held leases on property which they wished to test for oil. They estimated the cost of drilling a well to the depth at which it was believed oil would be found and then sought to finance the drilling by executing instruments like the one herein considered. After execution of the instrument, which stated the estimated drilling cost allocable to the undivided working interest transferred, they proceeded with the drilling. The

various participants were then billed for the amounts they agreed to pay to defray the drilling costs. But no sums were ever paid Sanders-Fye for a working interest as such, nor was it ever intended that anything was or ever would be due for such "interest."

Significantly, the plaintiffs treated all sums advanced by them as "intangible drilling and development costs" on their Federal income tax returns, not as payments for a leasehold interest, a security, or any other capital asset. Further, Hy Hammer and Morris Norian both declared that all money expended by them was pursuant to bills of Sanders-Fye for drilling (or in one instance, equipping,) costs.

Nor did Sanders-Fye consider the money as payment for a share in a working interest. Lenn Franke, who represented Sanders-Fye in some of the transactions, stated by affidavit that the plaintiffs contacted him relative to getting into the oil business and that he explained to them the operations of the Sanders-Fye Drilling Company. Among other things, he told them: "If you wish to join in the drilling of these wells or in any future wells, a proportionate share of the working interest in the lease covering the property where the well or wells are to be drilled, will be transferred to you at no additional cost, and in the event of a producing well, a proportionate interest will be assigned to you so that you can sell your share of the oil directly to the purchaser if you so desire." The plaintiffs nowhere assert that this does not correctly reflect their own understanding of the proposed ventures.

Now the first few ventures were successful, and the defendants executed written assignments to the plaintiffs. From these wells the plaintiffs received, and presumably

are still receiving, income proportionate to their shares in the leases. The plaintiffs never at any time questioned this procedure.

Piecing all this together, we believe the record shows that the development contract aspects of the instrument were uppermost in the minds of the parties. The only sums advanced by the plaintiffs were for drilling costs—not in payment of shares in working interests. The transfer of a working interest, even if it be assumed that it was effective immediately upon execution of the instrument, merely served as a basis for agreeing on the drilling of a test well and for establishing the plaintiffs' share of the oil, if and when produced. In effect, the parties, as co-owners of the working interest, were thereby enabled to form an association for oil development, with the ultimate profits to be distributed as their interests appeared. At best, the transfer of a working interest was incidental to the development contract.

Therefore, Hammer should not be entitled to recover the $242.19 expended by him in our illustrative transaction. For even assuming he *acquired* a "security" within the statutory definition, he did not pay the $242.19 for it. This money was paid for drilling costs in accordance with a development contract. Despite the purport of the instrument, which seems to contemplate the payment of an additional $242.19 for an undivided working interest in the leases, in point of fact no such additional amount was ever paid Sanders-Fye. Nor was such ever within the actual contemplation of the parties. In short, Hammer did not pay the stated consideration for the "security," or for that matter any sum of money, so there was no "amount paid" or "consideration given" for him to recover.

The statute contemplates the return of money expended in purchasing the "security," and it is the plaintiffs' burden to demonstrate a right to recover. In this regard, a basic distinction must be recognized here; namely, the difference between sums spent to *acquire the interest* and sums advanced to *exploit the property* (*i.e.*, test for oil and gas). If a group of people own undivided shares of a working interest, an agreement among them to develop that property is clearly not within the purview of the statute. These 45 transactions are, in substance, of the same type, even though the transfer of the interest and the entering into of the contract for drilling may be said to occur simultaneously. For while there were many ways Sanders-Fye and the plaintiffs might have arranged for the transfer of the interests and the drilling of the wells, they in fact utilized but one method. And that, as related above and as borne out by the records, was to transfer a share of the working interest to one who was willing to exploit that property with them by contributing a proportionate share of the estimated drilling costs. Sanders-Fye were not brokers, and they expected profits from oil production, not from selling working interests. All sums involved were advanced for and used in drilling, and this was fully understood by all parties concerned.

Even if we were compelled to judge the transactions without benefit of the practical construction given them by the parties themselves, as the minority apparently advocate, we would conclude no differently and our reasoning would be much the same. The instruments on their face call for two payments, one for an undivided working interest (second paragraph) and the other for drilling costs (third paragraph). The statute allows a recovery

for sums spent in purchasing the interests, but when it is shown that no such sums were in fact spent, the plaintiffs' case fails. While the statute has a wide scope and a worthy purpose, it should not be applied so as to permit the plaintiffs to recover money they expended as their share of drilling costs. Apart from the statute, there could not, in justice, be a recovery without proof of fraud, duress, or similar conduct justifying rescission. Nor as we view the matter can there be, by statute, any recovery under the circumstances here and as the issues have been presented for our decision. And while it is of no legal consequence, it is interesting to note that this is in accord with the position adopted by the Secretary of State at one time. The defendants allege, and plaintiffs do not deny, that they sought to register instruments of this type with the Secretary of State in 1936 but were informed by the then Secretary of State that the law did not require it.

Remaining for consideration are the six transactions, evidenced by invoices only, where there admittedly were sales or undivided working interests in producing wells. These clearly involved the sales of securities under our statute.

The defendants, however, question the sufficiency of the tender. They point out that the plaintiffs had received income from the wells which they did not tender, nor did they tender a written assignment, quitclaim deed, or any other written disclaimer of interest showing their relinquishment of an interest in the lease.

As to the first objection, the applicable statute contains no requirement that the income received be tendered, stating merely that "securities sold" be tendered. This was

changed by amendment in 1953, but the earlier statute governs here.

Nor was the tender otherwise insufficient. The sales were evidenced by invoices only, no written assignments having been made. In such case, the plaintiffs, both in a prior letter of rescission and in their complaint, made a sufficient tender by offering to return all that they had received. Their tenders were as formal as the evidence of sale, and under the circumstances all that could reasonably be deemed necessary.

For the reasons stated, the judgment of the Appellate Court is affirmed in part and reversed in part. The cause is remanded to the circuit court of Cook County with directions to enter judgments for the plaintiffs as to sums advanced pursuant to said six transactions where they purchased interests in leases, deny them recovery for any other sums paid the defendants, and to proceed in a manner not inconsistent with the views expressed in this opinion.

*Affirmed in part and reversed in part, and remanded, with directions.*

Mr. Justice Davis, dissenting:

I can neither concur with the reasoning of the majority which places the transactions before us beyond the scope of section 2 of the Illinois Securities Act, nor understand their failure to consider the charge of violation of the Federal Securities Act, as alleged in count II of the complaint and assigned as error and so argued by plaintiffs. These transactions cannot be placed outside the purview of the State or Federal Securities Acts without ignoring the plain language of the statutes and the clear economic import of the transactions.

The statutes are drawn in the broadest terms:

"The word 'securities' shall mean and include * * * investment contracts, * * * participation certificates, * * * certificates evidencing shares or interest in * * * associations, * * * or any contract * * * representing * * * evidence of * * * title to or interest in * * * property * * * of the Issuer thereof, and any oil, gas or mining lease, royalty, or deed, and interest, units or shares in any such lease, royalty, or deed * * * and any other instrument commonly known as a security * * *. The term 'sale' means and includes contracts and agreements whereby securities are sold, traded or exchanged for money, property or thing of value, or any transfer or agreement to transfer, in trust or otherwise." Ill. Rev. Stat. 1953, chap. 121½, par. 97.

"(1) The term 'security' means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment

contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a 'security,' or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing." U. S. Code, Title 15, chap. 2A, subchap. 1, par. 77b(1).

By the breadth of the language used, our congress and legislature, as well as the legislatures of other States, sought to bring the widest variety of economic speculation within the purview of regulation, and to avoid devious and ingenious schemes to circumvent the act. See Bloomenthal, SEC Aspects of Oil and Gas Financing, 7 Wyo. L. J. 49, 55 (1953); 46 Col. L. Rev. 885.

The history of the exploitation of oil and gas rights is one of great commercial and economic development with concurring wildcat speculation and fraudulent and deceitful promotions. "(It) has been accompanied by the creation of legal interests which are, in many respects, *sui generis*. The law relating to these interests combines familiar principles of the law of property, contracts, landlord-tenant, and tenancy-in-common; however, in no other field are they combined in the particular pattern and with the particular overtones that they are found in oil and gas law." Bloomenthal, SEC Aspects of Oil and Gas Financing, 7 Wyo. L. J. 49.

It was therefore reasonable and necessary that securities be defined so as to embrace every clear attempt to provide a type of "security" investment regardless of the peculiar legal form of the transaction. In a situation similar to the one before us, the Supreme Court of the

United States laid down a succinct but useful test, applicable here. "The test is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others." (*Securities & Exchange Com.* v. *Howey Co.* 328 U.S. 293, 301.) In view of the salutary purposes of regulatory securities legislation, the term "securities" has been given a broad and liberal construction. (*Securities & Exchange Com.* v. *C. M. Joiner Leasing Corp.* 320 U.S. 344; Anno. 163 A.L.R. 1050 *et seq.*) "The statutory policy of affording broad protection to investors is not to be thwarted by unrealistic and irrelevant formulae." (*Securities & Exchange Com.* v. *Howey Co.* 328 U.S. 293.) In determining whether a particular instrument is a security within the meaning of the statute, the substance of the transaction and the relationship between the parties will control as against the form of the alleged security. *Securities & Exchange Com.* v. *Universal Serv. Assn.* (C.C.A. 7th) 106 F. 2d 232; *certiorari* denied 308 U.S. 622.

I do not understand that my colleagues of the majority disagree with these principles, and indeed they admit that the instruments "on their face" are "securities" within the purview of the Illinois statute, and that the resulting transactions might lead one to believe that the money was paid for a working interest in the leases. However, I believe that these conclusions determine the question before this court. I find no "conflict between the import of the instrument and the parties' own understanding of its terms."

The letter agreement prepared by defendant, provided: "It is also agreed that you are purchasing this interest for investment purposes only without any present intention of

reselling this interest." This provision illustrates that defendants, sellers of the interests and drillers of the wells in question, recognized the transaction as a sale of a working interest, or lease, for it is certain that no one would purchase a share of the drilling cost of an oil well as an investment.

The letter agreement was artfully drafted by the defendants. It commences: "We will assign to you an undivided * * * working interest, under oil and gas leases * * * for the sum of ....." The letter continues with a usual and customary covenant as follows: "We agree to commence * * * the drilling of a well for oil and/or gas, to diligently prosecute the drilling of same and to test all possible oil formations * * * for the sum of ..... which is your share of the drilling cost of this well."

It is definite that the assignment is to be made for a certain sum, which is to be considered a share of the drilling cost. In clarification of the agreement, the letter further states that: "In the event of a producing well, it is understood and agreed that, in addition to the amount as set up above, you will pay your proportionate part of the casing, drilling in expense (etc.)."

The majority concludes that it was the agreement of the parties that only one sum was to be paid. I do not consider that this gives rise to an ambiguity, but rather believe that it expresses a reasonable understanding of the terms of the contract. The plaintiffs, who had no knowledge or experience in the oil business, clearly desired to provide venture capital which would be used for the drilling of an oil well in the anticipation that they would receive a royalty or leasehold interest in the oil produced. The defendants-promoters, on the other hand, obtained

money to finance their drilling operation in exchange for the promise of a portion of the anticipated oil profits. Clearly, this was a case of investment of money in a common enterprise by the plaintiffs with the anticipated profits to come solely from the efforts of defendants. (*Securities Exchange Com.* v. *Howey Co.* 328 U.S. 293. The instrument was a security under the definitions of the Illinois and Federal Securities Acts. Ill. Rev. Stat. 1953, chap. 121½, pars. 96-147, incl.; U.S.C. Title 15, chap. 2A, subchap. I, par. 77b(1).

The form of the instrument does not in any way change the obvious practical and economic relationship of the parties. As was said by the Supreme Court of the United States in *Securities & Exchange Com.* v. *C. M. Joiner Leasing Corp.* 320 U.S. 344: "It is clear that an economic interest in this well drilling undertaking was what brought into being the instruments that defendants were selling and gave to the instruments most of their value and all of their lure. The trading in these documents had all the evils inherent in the securities transaction which it was the aim of the Securities Act to end."

It seems to me that the majority has left the world of realism when they state that "the development contract aspects of the instrument were uppermost in the minds of the parties. The only sums advanced by plaintiffs were for drilling costs—not in payment of shares in working interests." The plaintiffs invested money, with the understanding that it would be used for drilling a well; but the drilling of the well, in itself, would benefit them not an iota unless they received, for that investment, a right to share in the oil benefits reaped by the drilling efforts of the defendants. There was no provision for further

payment for the acquisition of a "working share" but merely an agreement to pay certain set expenses upon production of oil.

However, even if we assume, as the majority hold that, "at best, the transfer of a working interest was incidental to the development contract," the majority conclusion is contrary to the provisions of the Illinois Securities Law which reads: "Any security given or delivered with, or as a bonus on account of, any purchase of securities or other thing of value shall be conclusively presumed to constitute a part of the subject of such purchase and to have been sold for value." (Ill. Rev. Stat. 1953, chap. 121½, par. 97(4).) Thus any working interest given or delivered with, or as a bonus on account of payments made for drilling costs, under the act is conclusively presumed to constitute a part of the subject of such purchase and to have been sold for value and constitutes a sale within the purview of the act. *Whittaker* v. *Hall,* 226 Fed. 2d 868.

There is nothing in the activities of these parties to detract from the clear language of their written agreement. The practical relationship between the parties is inescapable. The defendants had a lease and financed the exploitation of that leasehold interest by obtaining their drilling expenses in exchange for a conveyance of a working interest. Their gain was to be obtained without financial risk, by the retention of a substantial overriding interest. This was not a joint venture. There was neither provision for any control of the operation by the plaintiffs, nor for them to share in any losses of the venture beyond their initial investment.

I believe that the hyper-technical and basically imprac-

tical analysis of the majority has given rise to a simple method to circumvent the Securities Act and create a potentially powerful instrument for fraudulent promotions to bilk the public, and that the decision serves to judicially abrogate the clear language and intention of the legislature.

In my opinion, the fact that both parties sought to take advantage of the special provisions of the Internal Revenue Code does not militate against this view. The purposes and policies behind the deductions and exemptions allowed by our Federal tax laws are far different from those which form the basis of our State and Federal "Blue Sky" laws. Even though the Congress of the United States sees fit to permit the deduction of these expenses, this circumstance neither lessens the imminent danger of fraud which our Securities Acts were designed to prevent, nor aids in their construction. The tax treatment of these expenditures by the parties should not serve to abrogate a regulatory statute of this state or nation.

SCHAEFER and KLINGBIEL, JJ., concur in the foregoing dissenting opinion.

## APPENDIX C.

**Counts of Complaints Which Raised Federal Question.**
(R. 2:7-8.)

COUNT II.

Plaintiff, H. C. Hammer, states that:

1. Plaintiff realleges paragraphs 1, 2, 5, and 6 of Count I as paragraphs 1, 2, 3 and 4 of this Count II as though here fully set forth.

5. The said instruments of which the exhibits attached hereto are copies and the interests represented and evidenced thereby are and at all times mentioned herein were securities as defined in The Securities Act of 1933, and at no time have they been securities classified as exempt under that Act, nor were said sales such as are classified as exempt under said Act. The right to sell said securities in the United States was not at any time granted to defendants. Neither preceding the sales nor during the sales or negotiations for the sales did defendants or any other person procure an express or implied authorization from the Securities and Exchange Commission of the United States of America to sell the securities, nor at any time theretofore or thereafter did defendants or any one in their behalf comply with the requirements and provisions of said Securities Act of 1933 or the regulations promulgated thereunder with respect to the sale or offering for sale of the securities, nor file or register in the Office of the Securities & Exchange Commission any statements or documents required by said Securities Act of 1933 or regula-

tions. In effecting said sales to plaintiff, defendants made use of the United States mails and the means or instruments of transportation and communication in interstate commerce. All of the defendants in violation of the provisions of said Act knowingly authorized, aided, and assisted in the furtherance of the unlawful sales of said securities to the plaintiff.

WHEREFORE, plaintiff, H. C. Hammer, asks judgment against the defendants in the sum of $40,328.18 plus costs.

/s/ H. C. HAMMER,
*Plaintiff.*

Verification.

The corresponding counts of the complaints of petitioners Morris Norian and Richard Norian (R. 2:54-55 and 2:74-75) are identical in substance.

## APPENDIX D.

**Judgment of Illinois Supreme Court Sought To Be Reviewed.** (R. 20-21.)

(Order Entered on March 22, 1956. Rehearing Denied on May 22, 1956.)

And now, on this day, this cause having been argued by counsel, and the Court having diligently examined and inspected as well the record and proceedings aforesaid, as matters and things therein assigned for error, and now, being sufficiently advised of and concerning the premises, for that it appears to the Court now here, that neither in the record and proceedings aforesaid, nor in the rendition of that part of the judgment of the Appellate Court, First District, as to the forty-five transactions based on so-called letter agreements is there anything erroneous, vicious or defective, and in that part of the record there is no error.

Therefore, it is considered by the Court that the part of the judgment of the Appellate Court, First District, as to the forty-five transactions based on so-called letter agreements aforesaid, be affirmed in all things and stand in full force and effect, notwithstanding the said matter and things therein assigned for error.

And it is further considered by the Court that in the rendition of that part of the judgment of the Appellate Court, First District, as to the six transactions evidenced by invoices only, there is manifest error.

Therefore, it is ordered by the Court that for that error and others in the record and proceedings aforesaid, the

judgment of the Appellate Court, First District, as to the six transactions evidenced by invoices only, in this behalf rendered, be reversed, annulled, set aside and wholly for nothing esteemed, and this cause be remanded to the Circuit Court of Cook County with directions to enter judgments for the plaintiffs as to sums advanced pursuant to said six transactions where they purchased interests in leases, deny them recovery for any other sums paid the defendants, and to proceed in a manner not inconsistent with the views expressed in the opinion attached to this mandate.

And it is further considered by the Court that the said appellants recover of and from the said appellees costs by them in this behalf expended, to be taxed, and that they have execution therefor.

Office - Supreme Court, U.S.
FILED
SEP 12 1956
JOHN T. FEY, Clerk

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1956.

**No. 323**

H. C. HAMMER, MORRIS NORIAN AND RICHARD NORIAN,

*Petitioners,*

*vs.*

CHARLES W. SANDERS, JOHN L. FYE AND O. R. THOUREEN, INDIVIDUALLY AND AS CO-PARTNERS DOING BUSINESS AS THE SANDERS-FYE DRILLING COMPANY,

*Respondents.*

## BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

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THE BUNTHORP-WARREN PRINTING COMPANY, CHICAGO

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### CITATIONS TO OPINIONS BELOW.

A previous opinion in the lower Illinois Appellate Court is reported in 6 Ill. App. 2d 346.

### STATUTES INVOLVED.

In addition to those portions of the Federal Securities Act of 1933 cited by Petitioners, these sections are deemed material to this proceeding:

1. Section 3(a)(11) of Title I of the Federal Securities Act of 1933, 15 U. S. C. 77 *c*(a) (11):

Exempted securities

(a) Except as hereinafter expressly provided, the provisions of this subchapter shall not apply to any of the following classes of securities:

* * * * *

(11) Any security which is part of an issue sold only to persons resident within a single State or Territory, where the issuer of such security is a person resident and doing business within or, if a corporation, incorporated by and doing business within, such State or Territory.

2. Section 12 of Title I of the Federal Securities Act of 1933, 15 U. S. C. 77 *l*:

Any person who—

(1) sells a security in violation of section 77 *c* of this title * * * shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for said security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damage if he no longer owns the security.

## STATEMENT OF THE CASE.

There is no dispute but that Petitioners and Respondents entered into a series of agreements. In their statement of fact, Petitioners label these as sales of undivided interests in oil and gas leases. That was the factual question involved in the various appeals. Fairly phrased, the conflict of fact is whether or not the dollar amounts mentioned in each letter agreement was spent to acquire an undivided interest in an oil and gas lease or to purchase the services necessary to drill an oil well.

Only for purposes of these suits have Petitioners claimed that the instruments represent the sale of interests in oil and gas leases. In testimony (R. 2; 149, 141) and in income tax returns (R. 2; 157) Petitioners took the position that the amounts expended for which recovery was sought were for drilling costs and not for costs of acquisition of securities.

Further facts having an important bearing on this ap-

peal are the undenied facts that only seventeen persons, all of whom were residents of the State of Illinois, participated in the transactions of which complaint was made (R. 2: 178, 181).

Petitioners received and continue to receive payments on the very transactions which they have sought to rescind (R. 2: 150, 152, Petition, Appendix B, x, xi). The amount for which judgment entered was for the entire amount claimed to have been expended for the so-called "securities."

## ARGUMENT.

### I.

The opinion of the Illinois Supreme Court pointed out that the only question presented to it involved a violation of the Illinois Securities Act. As stated by that Court (Petition, App. B, vi, vii, 8 Ill. 2nd 414 at 418):

> "By their complaints, filed in February, 1953, the plaintiffs sought to rescind the transactions and recover all sums expended by them. They alleged a violation of both the Illinois Securities Act of 1919 and the Federal Securities Act of 1933. The defendants disputed their right to recover, *and as presented and argued in the briefs and on oral argument, the determinative issue is two-fold: (1) Were the instruments or interests involved securities which were sold in violation of the Illinois statute?* (Ill. Rev. Stat. 1953, chap. 121½, par. 97.) *(2) If so, did the plaintiffs make proper statutory tender?* (Ill. Rev. Stat. 1953, chap. 121½, par. 132.)" (Emphasis supplied.)

The opinion is of course decisive as to what issues were presented to and decided by that Court. The effect of the opinion is to declare that the Petitioners had abandoned or waived their position with reference to the Federal Securities Act.

Rule 39 (1)IV of the Illinois Supreme Court emphasizes that "A point made but not argued may be considered waived."

The claimed violation of Federal law having been waived or abandoned under the State practice, this Court will not refuse recognition of the effect of that practice.

Justice McKenna in *Hulbert* v. *City of Chicago*, 202 U. S. 275, 26 S. Ct. 617, 618, announced the Court's adherence

to Illinois' Rules of Practice in a case originating in Illinois:

> "According to the practice of the court, an error not assigned is not open to review. *Berry* v. *Chicago*, 192 Ill. 154, 155, 61 N. E. 408. Errors assigned, but not noticed or relied on in the brief or argument of counsel, will be regarded as waived or abandoned. *Keyes* v. *Kimmel*, 186 Ill. 109, 114, 57 N. E. 851. And such rule of practice will be recognized by this court. *Erie R. Co.* v. *Purdy*, 185 U. S. 148, 153, 46 L. ed. 487, 850, 22 Sup. Ct. Rep. 605. It follows that this court has not jurisdiction of this writ of error."

To the same effect is *Hiawassee River Power Co.* v. *Carolina-Tennessee Power Co.*, 252 U. S. 341, 40 S. Ct. 330.

## II.

It may be less than satisfying to show the existence of the waiver or abandonment without showing the reasons therefor. In order to show this Court that no injustice is being done Petitioners on this score it is only necessary to refer to those facts which would prohibit any judgment under the Federal Securities Act from being entered. These facts are uncontroverted in the record.

Petitioners, Respondents, and all members of the group which participated in the transactions of which complaint was made were residents of the State of Illinois (R. 2: 178, 181). The number of persons involved totalled seventeen (R. 2: 178, 181). Under the Federal Securities Act, Section 3 (15 U. S. C. 77 c) provides the following pertinent exemptions even if the transactions were classified as "security" transactions:

> "(a) Except as hereinafter expressly provided, the provisions of this subchapter shall not apply to any of the following classes of securities:
>
> * * * * *

> (11) Any security which is part of an issue sold only to persons resident within a single State or Territory, where the issuer of such security is a person resident and doing business within, or, if a corporation, incorporated by and doing business within such State or Territory."

These Petitioners are asking this Court to review a Federal question which on the uncontroverted facts could not but result in a judgment for the Respondents. The explicit exemption granted "intrastate" transactions bars any recovery under the quoted section.

Presumably to negate the damaging impact of these facts, Petitioners have inserted in their Petition (pp. 10, 11) a suggestion that only affidavits are controlling on motions for summary judgment. By use of this technical exclusion, Petitioners seek to obscure and eliminate from this Court's consideration the undenied truth of Respondents' sworn allegation that all members of the group were residents of the State of Illinois.

The method is of even more dubious propriety when Petitioners recite, as Illinois law, that affidavits alone are controlling on motions for summary judgment. This proposition is not sustained by the cases cited in support thereof. The law in Illinois is that the "whole record must be considered" on summary judgment. *Sampson Co.* v. *Mandel Bros. Inc.*, 3 Ill. App. 2d 92, 95; *Gliwa* v. *Washington Polish Loan & Building Association*, 310 Ill. App. 465, 471. Only "if it appears from facts stated in affidavits or documents that the answer pleaded is sham or false or frivolous" will it be disregarded. *Gliwa* v. *Washington Polish Loan & Building Association, supra*, p. 470. These, the controlling tests under Illinois law, dictate the conclusion that the facts constituting an absolute bar to any recovery under Federal law must be recognized. Once so recognized, no

ground exists to predicate a violation of a Federal right and certiorari must be denied.

## III.

The petition for certiorari should be denied for still another reason. Petitioners have failed to specify, as required by this Court's rule 23 1.(f), the manner in which the federal question sought to be reviewed was raised in the Illinois Appellate and Supreme Courts; the method of raising that question in those Courts; and the way in which the question was passed upon by them.

These omissions are of the utmost significance in view of the previously described waiver or abandonment and in view of the limited scope of the opinion of the Illinois Supreme Court.

This same limited scope was dictated by the Petitioners' own theory of the case. Among the claims of Respondents was that the judgment was in error because Petitioners had judgment for the entire amount of their expenditures and still retained the income from the producing wells (R. 2: 150, 152, Petition, Appendix B, x, xi; 8 Ill. 2d 418). The Federal Securities Act (Section 12 of Title I, 15 U. S. C. 77 *l*) authorizes recovery only of the amount paid *less* income received on the "securities." Thus, the judgment for the full amount was congruous only with Petitioners' position with reference to the Illinois law and not with Federal law.

There is further internal evidence that the judgment of the trial court was predicated solely on Count I, the count under the Illinois Securities Act. The sixth paragraph of the judgment order (R. 2: 186) provides:

> "That consideration of the matter of plaintiff's reasonable attorneys' fees herein pursuant to statute in such cases made and provided is hereby reserved."

*Only* the Illinois Securities Act permits recovery of attorneys' fees (Ill. Rev. Stat. 1953, chap. 121½, par. 132 (l)). The Federal Statute, Section 12 of Title I of the Federal Securities Act of 1933; 15 U. S. C. 77 *l*, contains no warrant for attorney's fees.

Having accepted the larger benefits available under Illinois law, Petitioners may not now contend that the reversed judgment was rendered in conformity with Federal law. A corollary to this proposition is that Petitioners may not urge that the reversal of the judgment founded on Illinois law infringes any Federal right.

## CONCLUSION.

Only by abandoning the shores of fact for the seas of fiction is even a semblance of worthiness attained by Petitioners' arguments. Pumping the water out of Petitioners' specious arguments, we have only a decision on a point of Illinois law which the Illinois Supreme Court is well equipped to decide. The Illinois Court's opinion has effect only in deciding the internal law of this State. Respondents are without knowledge as to the dire effects predicted so freely by Petitioners but suggest that the Illinois legislature is the place to voice those fears. No Federal law, no intent of Congress has been transgressed where the grounds for decision were state grounds and were so specifically limited by the deciding Court. Yet, in reading the Petition for Certiorari, the feeling is forced that Petitioners have sought to mislead this Court as to what was actually decided and have failed to bring to this Court's attention those facts which would preclude its review.

Because the opinion of the Illinois Supreme Court was

concerned solely with interpretation of Illinois law and because an absolute exemption to the operation of Federal law exists, the petition should be denied.

We respectfully urge that the petition for a writ of certiorari should be denied.

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